No. 200 BULLETIN OF THE AGRICULTURAL COLLEGE EXTENSION SERVICE, THE OHIO STATE UNIVERSITY June, 1939

Borrowing by Farmers

When? Where? How?

SHOULD THE FARMER BORROW?

The old-time farmer who struggled for years to pay the mortgage on his farm was likely to say "Never again." If the borrowing is to go into immediate consumption or into a better car than one can afford, maybe he would better stick to that motto a while longer.

If he is borrowing to add to a farm too small to be an economical operating unit, to buy feeders which will market his corn and pasture to advantage, to buy fertilizer or spray materials, or otherwise to improve his operating efficiency, mayhap the motto no longer holds. Here is the place for a careful figuring of probable gains against costs and possible losses.

CAUTIONS TO OBSERVE:

1. Monthly payment plans are unsuited to most farm enterprises.
2. Avoid any loan whose interest and other costs are above the average return of the enterprise proposed.
3. In long-time loans, avoid frequent renewals.
4. In small loans, costs of placing the loan add rapidly to interest rate.
5. Be sure, before you accept and sign for the loan, that you understand all the terms.
6. Beware of heavy debt and interest. Better, too, to have sufficient capital to operate well a rented farm than to so reduce that capital in making first payment on a farm as not to be able to operate the farm efficiently when you have it.

But don't lose the opportunity to operate with greater efficiency, when borrowing what you can repay will make money for you.

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Issued in furtherance of Acts of Congress dated May 8 and June 30, 1914

Long Time Loans

Why May One Want a Long-Time Loan?

One may be planning to buy a farm; he may plan to build a modern residence and/or other costly buildings on his farm; a number of debts, no one of them very large, may together be more than can be paid out of a year's or even two or three years' income on the farm. In such a case, he will need a loan to be paid out gradually over perhaps a long period of years.

Security he will offer — a first or second mortgage on his farm.

I. -- Agencies Sponsored by the Federal Government:

Where will he get such a loan?

1. NATIONAL FARM LOAN ASSOCIATIONS — Local associations of farmers, whose loans are made finally by the Federal Land Bank, or the Land Bank Commissioner. The Land Bank loans are drawn up at 4 per cent, require first mortgage security, are limited to 50 per cent of the appraised value of the farm and buildings, and are payable over a 25- to 34½-year term without necessity of renewal. The Commissioner's loan is at 5 per cent interest, is payable in 10, 20, 30, or 40 years, and cannot go beyond 75 per cent of the appraised value of the farm. In case a Commissioner's loan is granted, the Federal Land Bank takes the loan up to 50 per cent of the appraisal and the remainder of the loan is a Commissioner's loan.

There is considerable delay and uncertainty in placing the loan; the initial cost of abstract, appraisal, etc., is high (though when divided over 33 years the yearly cost is not high); a borrower must take stock in the farm loan association to an amount equal to 5 per cent of his loan, and he may or may not be able to apply this stock in making the last payments on the loan. On the other hand, there are no renewal costs, the interest rate is low, no large payments are required at any time; and the borrower becomes a part in building up a farmer-owned credit agency.

2. FEDERAL HOUSING ADMINISTRATION — Does not loan directly, but insures loans made by acceptable financing agencies. These loans at 5 per cent per year interest and up to 20 years maturity may be:

a. To buy and improve farms by modernizing or constructing farm houses and other buildings.

b. To refinance mortgages and construct or modernize farm buildings.

NOTE: 15 per cent of the loan must be used for materials and labor for new construction or repairs.

These loans carry a higher rate than land bank loans; each payment, too, must include interest, payment on principal, taxes, insurance on buildings, and an added ½ per cent as loan insurance premium. The loans, however, may be up to 90 per cent of the appraisal if the appraisal is not above $6000, and 80 per cent of the further amount up to $10,000. Loans on property for owner occupancy and below $5400 may run for 25 years. The loan and all transactions may be with one's local bank.

3. The Farm Security Administration — Makes one type of long time loans, to a limited number of farm tenants or laborers in selected counties to enable them to buy farms, and make needed improvements. These loans are not refinancing loans.

The borrower agrees to carry out a plan of farm and household management carefully worked out with FSA and County Extension Service. The rate of interest is 3 per cent, but the borrower pays 4.32 per cent, which is sufficient to extinguish the loan within the time limit of 40 years. After 5 years, the borrower may repay the balance at any time, or as rapidly as he wishes. Only a limited number and those in certain counties of the state can be served under this plan, but the fortunate ones have a low rate, long time with no renewal costs, assistance in working out management plans, and a loan which may go as high as 100 per cent of appraisal.

II. -- Private Agencies

1. The Seller — Frequently the best terms for a loan — length of time, rate of interest, payment plan — can be gotten from a seller anxious to sell and acquainted with the buyer. The possible disadvantage is that the death of the seller or a change in his plans may result in considerable pressure on the buyer to pay off the loan at once.

2. The Local Bank — During 1930-34 many banks were forced out of long-time lending; but with increasing deposits, better business outlook, and more liberal legislation, many banks are actively seeking long-time farm loans.

The bank will require a higher rate of interest than federal agencies. Loans will seldom be drawn for more than three years, and while in general renewals are granted so long as interest and some reduction of principal are kept up, the borrower must recognize that the bank can and may demand payment at maturity. On the other hand, service is prompt; one confers personally with the lender; the lender, too, is in touch with local conditions and may be more lenient.

3. Insurance Companies — Many of the larger insurance companies offer today farm mortgage loans of 5, 10, 15, and even 20 years' duration. The rate of interest varies among companies and with the risk; we hear of rates of 4¼, 4½, 5, and 5½ per cent. One company loans at 4½ per cent when the loan does not exceed 50 per cent of the appraisal, at 5 per cent if the loan is 50 to 60 per cent of appraisal, and at 5½ per cent if the loan is 60 to 70 per cent of appraisal. One who borrows directly from the company agency in some large city pays no fee for placing or renewing the loan; local representatives generally charge a fee for this service.

4. Building and Loan Companies — Normally loan on city properties and to those who can make monthly payments. Outside the large cities these companies also make farm loans. Payments are semi-annual; the rate is 6 per cent on the balance remaining at any time. The plan generally offered calls for the loan's paying out in not quite 12 years, but sometimes 15-year loans are made. The rate is higher than that of the Land Banks, but the service is prompt, and the lender is near at hand for conference at any time.

Short Time Loans

The money to be borrowed may not require a long period of years to repay. The loan may be of the self liquidating type like money for seed, fertilizer, or labor, and to be repaid when the crop is sold; or for a car of feeder cattle or lambs, and to be repaid when this stock is sold. It may be for building repairs or for new fences or implements, or for additions to work or dairy stock. It may be of emergency nature, due to an accident, the death of a needed work animal, or even illness of a member of the family. All such loans are normally paid off within 12 months, or renewed at lower amounts for final extinction in the second or third year.

Of the many sources available, which suits the borrower's conditions best?

I. -- Federally Sponsored Agencies

1. Production Credit Associations — Ohio is divided into 12 districts, each served by one of these associations. They were set up in 1934 as a part of the Farm Credit Administration, and designed to make short-time loans for almost any farm purpose or emergency. Nearly all loans are based on the security of farm livestock and/or implements, and they may cover crops also.

The main disadvantages of these loans are the delay and possible rejection after delay; and the inspection costs which on small loans materially raise the percentage of cost. (On large loans this cost of placing the loan may be less than ½ of 1 per cent.)

On the other hand, the low interest rate (at present 4½ per cent per year), the payment plan carefully adjusted to the dates and amounts of probable income, and the opportunity of building up a farm credit organization owned by farmers, are decided advantages.

Note: There are an agricultural association and several livestock associations which make loans similar to PCA loans and on quite similar terms.

2. Farm Security Administration — In addition to the long-time loans described on page 3, the FSA makes short-time loans to many farmers unable to secure loans elsewhere. The loans may be of the self-liquidating type and to individual farmers. A farmer may be burdened with a load of debt beyond the ability of himself and his farm to pay. The FSA Farm Debt Adjustment Service will attempt to help him secure an adjustment of his debts, and if the adjustment results in bringing the debt total within the probability of payment, a loan may be made. Another type of loan is the so-called Community and Cooperative Service loan, to enable several farmers to have the use of a binder, a drill, a livestock sire, which no one of them singly could afford. This loan may be made to the group, or to one of the group who has a contract for use with the others of the group.

The farm family receiving any of these loans must agree to operate the farm and the home under management plans worked out by the family and the

FSA and County Extension Service. The rate of interest is 5 per cent, and payments are adapted to the times of probable farm income.

3. FEDERAL HOUSING ADMINISTRATION — Does not itself make loans but encourages lending by banks and other financial institutions by insuring them against losses. The loans insured may be loans for improvement of city, suburban, or farm real estate. Insurable loans may be for repairs, alterations, improvements, and for the installation of built in or permanently attached features, such as heating, lighting or plumbing systems, cupboards, closets, wells, cisterns, walks, driveways, fences, garages, barn or barn improvements, poultry houses, machinery sheds, etc.

The loan is arranged through one's local bank, or often the dealer has arrangements through some bank. The law authorizes loans for a period of five years. The rate is 5 per cent per year added to the face of the original obligation (which approximates 9.7 per cent on the balance one owes at the various payment dates). Arrangements can be made for payments monthly, or at 3, 6, or 12-month intervals.

4. COMMODITY CREDIT CORPORATION — Makes loans to producers on wheat, corn, wool, tobacco, and other agricultural products designated by the President. The commodities used as security must be stored in accordance with the regulations; in case of corn and wheat the regulations have permitted storage either in an approved public warehouse, or in the farmer's own bins or cribs under the Farm Warehousing Law. The borrower must have agreed to produce his crops in accordance with the Federal agricultural program.

These loans are used partly to enable the farmer to hold his products for future sale or future use; they also, through a guarantee of taking the security at the loan value, are sometimes used to bolster the price of the product, as no farmer will sell his grain at less than the guaranteed value.

The rate of interest charged is 4 per cent per year. The maturity date varies and is in accordance with the terms set forth in announcing each loan.

5. RURAL ELECTRIFICATION ADMINISTRATION — Makes loans to rural electric cooperatives —

a. For the building of their electric lines.

b. For advances to farmers for the wiring of their houses.

These loans to farmers are at 5 or 6 per cent as decided by the local cooperative.

Some local electric cooperatives make loans to their members for the purchase of electric equipment, in turn rediscounting this paper with the Electric Farm and Home Authority; others advise their members to borrow from the PCA or the Farm Bureau A. C. Association.

6. THE EMERGENCY CROP AND FEED LOAN OFFICE — Makes loans to farmers for crop and feeding purposes where such credit is not available through other agencies. Many farmers availed themselves of this service in the early 30's, but now (1939) fewer than 1 per cent of central Ohio farmers are using this source of funds.

II. -- Private Agencies

1. The Local Commercial Bank — The primary purpose of the local bank is the making of short-time loans. It is more and more coming back into the farm lending field.

The rate of interest is higher than charged by some agencies (commonly 6 or 7 per cent per year, with certain types of loans, and in some areas at 5½ or even 5 per cent). The borrower generally has to sign a 90-day note (the oral understanding of probable renewal is generally realized, but the signer of a 90-day or demand note must never forget that payment may be enforced as the terms provide). The convenience, informality, and promptness of service, the personal acquaintance of lender and borrower, the adaptability to varying conditions, the low expense of placing the loan, are some of the advantages of this source of loans.

2. "Finance Companies" — These companies operate under the "Chattel and Salary Loan" law. They are set up primarily to make loans to those whose income is adapted to monthly payments, but they may, and several do, make loans calling for payment quarterly or even at convenience. The loans to farmers are on the security of farm livestock, implements, autos, household goods. The rate of interest on any amount below $300 may legally be as high as 3 per cent per month; usually the rates are 3 per cent per month on the first $150 or $200; 2 per cent per month on the remaining amount up to $300; and 8 per cent per year on any amount loaned above $300. Several companies loan on a so-called 11 per cent rate, which actually figures out at more than 20 per cent on the balances owed.

The main objection to this type of loan is the high rate of interest; no farm enterprise will normally earn half or a third of that rate. The place of this type of loan in farm life is to meet a temporary emergency and to be paid off as quickly as possible. On the other hand, it has most of the advantages described above for the bank loan — promptness, little or no charge for placing the loan, local representative whom the borrower can contact personally, and often considerable leniency in execution of terms.

3. Credit Union — A credit union is a cooperative agency designed to make small loans to its members on their personal credit, though it may require chattel or other security when it sees fit. The place of the credit union is in loans made to someone known to the credit committee, so that the loan can be placed with little or no placing costs. Normally any loan above $150 or $200 can be gotten elsewhere more cheaply than from any credit union charging the legal 1 per cent per month interest; however, most of the credit unions operating in rural Ohio charge only ½ per cent interest per month.

4. Mercantile Credit — Credit by the seller of the merchandise may be extended for months with no charge either in price or interest; or it may be an instalment sale that costs one 10 to 30 per cent per year or more on the balance he owes.

The phrase "pay as you use" is the one in vogue just now. It seems as reasonable to pay for a refrigerator or washing machine over a period of months as for a farm or dwelling house over a period of years. But once in use, the phrase is being played up by sales and finance groups to an utterly unwarranted degree.

It is one thing to apply it to durable goods, another to "soft" or immediately consumable goods; one thing to apply it to paying for a thing one needs, another to apply it to what one cannot afford, but was persuaded to buy under super-salesmanship devices; one thing to apply it to one or two pieces of needed equipment at a time, another to allow salesmen and lenders to tie one up to so many regular payments that the family's needs for food and clothing cannot be met.

Hence, to use instalment buying intelligently one must use his pencil; he must carefully estimate what his probable expenses for living will be, make some allowance for possible emergencies, and then if by economy he can pay so much per month for some needed piece of equipment, "pay as you use" has a legitimate place.

Another place to use a pencil is in figuring the terms. Terms in general are more liberal than they were five years ago, but at that "things are not what they seem." That is, most of the "instalments at 6 per cent" or "½ per cent per month" mean that ½ per cent is added to the original debt for each month the instalments run, which figures out at more than 11 per cent per year on the balances one owes. See illustration No. 1 below.

"Pay as you use," like dynamite, has its place.

Illustrations of Installment Sales

The note which one gives in an instalment purchase is secured by a chattel mortgage on the article bought. If the dealer handles his own paper, he frequently keeps this mortgage in his own files to use only in the case of necessity. If he sells the note to a bank or finance company, the mortgage is filed in the County Recorder's office, and when the buyer has paid his note in full, he should make sure that his credit record is cleared at the Recorder's office.

In calls on nine dealers, eight different plans were found, five of them being modifications of the ½ per cent per month plan. Among these plans were the following:

1. Assuming that I owe a $600 balance on a car, that I agree to pay in 18 equal monthly instalments, and that insurance on the car for the period is $50, one company figures thus: $600 plus $50 insurance is $650. 18 months interest at ½ per cent per month is 9 per cent. 9 per cent of $650 is $58.50. $650 + $58.50 is $708.50. So I pay each month one-eighteenth of $708.50, or $39.37.

2. One company selling electric washers and ranges claims, and truly, that the costs of bookkeeping, collection, and risk are relatively higher on small amounts. The following illustrates these terms, with the figure in each case showing the interest one is paying on balances owed:

On a $ 60 debt, 12 payments of $ 5.60 or $ 67.20 — about 22% interest.
On a $100 debt, 12 payments of $ 9.08 or $108.96 — about 16% interest.
On a $200 debt, 12 payments of $17.75 or $213.00 — about 12% interest.

3. Another adds 10 per cent as a carrying charge whether it is 24 months on a refrigerator or six months on tires or clothing. Reason — a refrigerator

used 12 months can, if necessary, be repossessed with almost no loss, while a tire used for even three months would seldom sell for the balance due. Ten per cent added figures at about 9.6 per cent interest on a 24-month deal, and about 34 per cent on a six-month purchase of tires.

4. Another firm selling tires adds 8 per cent to the balance due if payment is made in six monthly payments; this figures up to about 28 per cent interest on balances due.

If one wishes to borrow the money, one widely advertised loan is for 12 payments of $9.25 monthly on each $100 borrowed, or nine payments of $12 each — which are respectively about 20 and 19 per cent on balances owed.

Our purpose in presenting these illustrations is not that of criticism. There are heavy costs incident to monthly collections over 6 to 30 months — bookkeeping, follow-up letters, sometimes personal visits and repossessions; normally, the dealer would far rather sell for cash at — say — $200, than $210 or $220 over a period of time. Our purpose is to point out the costs of this method of buying, and the wisdom of the farmer's going to his bank or farm credit organization and borrowing at the 4½ to 6 per cent interest which they charge.

What to Do Before Interviewing the Lender

1. Know how much you are going to need, and when.

Go over your whole situation for the entire period of the loan. Think of all the things for which you will need money for farm operation and for living. A lender may be lenient with regard to expense of sickness or accident, but he should be able to assume that your list of normal expenditures is complete.

2. Know what you own and what you owe.

A business statement is merely a list of what you own — farm, stock, machinery, tools, seed, and feed, and any other property — all entered at fair but conservative values, and accompanied by a similar list of what you owe — farm and chattel mortgages, if any, other notes you are to pay, and what you owe at store or elevator, or to a neighbor. If you have paid any chattel mortgages or machinery notes in the past three years, be sure to see that they are no longer on file against you at the Recorder's office. You do not want the man from whom you are seeking a loan to think you are careless about your credit standing.

3. Have a plan of payment.

Lenders may demand security, but they are primarily interested in how the debt is to be paid. They do not lend if there is any probability that they will have to seize the security. The would-be borrower not only stands a better chance of obtaining his loan, but — more important still — is more likely to be borrowing intelligently and in line with his own interests, if he has carefully listed his probable sales of farm products and his other sources of income, with their approximate dates and a conservative estimate of what they will bring. He thus works out his farm management program, and also adds materially to the likelihood of getting his loan.

NOTE: Your county agricultural agent will be glad to tell you where to find any of the above loan agencies in your county.